Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Special Access Rates for Price Cap Local Exchange Carriers	)	WC Docket No. 05-25
	)	
	)	

REPLY COMMENTS OF THE UNITED STATES TELECOM ASSOCIATION ON THE NOTICE OF PROPOSED RULEMAKING

Several customers of special access services filed comments in response to the Notice of Proposed Rulemaking (NPRM)[1] alleging problems with competition and arguing for renewed regulation of special access prices.[2] It is apparent, however, that those comments do not offer any meaningful evidence against the position of the United States Telecom Association (USTelecom)[3] and its members that special access markets are increasingly competitive and that the Commission's pro-competitive policies are working well.[4] Instead, the special access

[1] *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Order and Notice of Proposed Rulemaking, 20 FCC Rcd 1994 (2005).

[2] *E.g.*, Ad Hoc Telecommunicaitons Users Committee Comments, at 35-50; American Petroleum Institute Comments, at 9; AT&T Comments, at 5-6; ATX/BridgeCom/Broadview/Pac-West/ US LEC/U.S. Telepacific Comments, at 17-32; Broadwing/Savvis Comments, at 22-32; BT Americas Comments, at 4-7; CompTel/ALTS/Global Crossing/NuVox Comments, at 20-30; Ionary Consulting Comments, at 4-10; NEXTEL Comments, at 17-28; PAETEC Comments, at 10-19; T-Mobile Comments, at 18-25; WilTel Communications, at 16-19; XO Communications, at 12-14.

[3] The United States Telecom Association used the name USTA when it filed its Comments in this proceeding, so those comments are referred to as USTA Comments. USTelecom is the same entity as USTA, and the USTA Comments are attributable to USTelecom.

[4] *E.g.*, BellSouth Comments, at 13-46; CenturyTel Comments, at 2-5; Iowa Telecom/Valor Comments, at 8-15, 21-37; SBC Communications Comments, at 9-57; USTA Comments, at 6-14, 16-19; Verizon Comments, at 5-35, 40-48.

customers arguing for increased regulation simply want prices lower than they can obtain in today's competitive markets.

It is perfectly natural for customers to seek lower prices; who wouldn't want the government to dramatically reduce the prices we pay for major purchases? It is just as appealing a concept as was a "chicken in every pot." While government-mandated price reductions in competitive markets may be a natural enough wish of purchasers, however, it is clear that society is not served well when government supplants the market and attempts to produce a politically-desirable outcome itself.

The Commission should reject the calls in this proceeding for central planning of special access markets. Many firms are offering competing special access services, and the market shares of special access entrants are growing. In sum, as will be explained below, the evidence in this proceeding is consistent with competition, and inconsistent with monopoly pricing. Rather than attempting to show unjust or unreasonable prices in any principled manner, parties seeking lower prices have done little more than complain that providing special access services is difficult and costly,[5] and allege that there are problems with competition because competitors haven't built out fully redundant networks to connect locations in the hope that some customers will choose to change providers at some point in the future. Instead, competitors are building to meet demand, which is reasonable in a competitive market.

USTelecom set out four recommendations in its Comments: (1) continue to foster competitive investment and entry by preserving current price caps, rather than deterring investment and entry through re-initialization or other manipulation of current rates; (2) increase

[5] Ad Hoc Users Comments, at 32-35; American Petroleum Institute Comments, at 5-6; Broadwing/Saavis Comments, at 11-14; NEXTEL Comments, at 10-11; WilTel Comments, at 7-8.

pricing flexibility by allowing providers to enter into commercial arrangements everywhere to better serve customers individualized communications needs as part of the transition to a free market; (3) decline to adopt a productivity factor to manage future earnings, as the inevitable mistakes can only harm the public interest; and (4) decline to prejudge the outcome of this proceeding by adopting interim rules, which are absolutely unwarranted.[6] These four recommendations are even more appropriate in light of the evidence submitted by parties.

I. THE EVIDENCE OF COMPETITION IS STRONG AND LARGELY UNREBUTTED

Many entrants are competing in special access markets, as amply demonstrated by the comments submitted in response to the NPRM,[7] and these entrants are winning many contracts and establishing meaningful and growing market shares. This special access competition is occurring throughout the country via traditional wireline alternatives and inter-modal competitors and, increasingly, most special access customers are able to choose from among several providers' offerings when entering into new contracts or buying new circuits out of tariffs. Moreover, both competitors and customers alike are often able to build, and many routinely do build, their own special access circuits. In fact, competition is so developed that even the party that originally petitioned for special access re-regulation—AT&T—does not seek re-regulation of OCn services.[8] Instead, AT&T focuses on the market for DS-1 and DS-3 end-user channel termination services, which often are dedicated to individual customers.

The ability to offer DS-1 and DS-3 competition is also widespread, as shown by BellSouth, SBC, and Verizon, despite AT&T's arguments in favor of regulatory price reductions. The Commission's current triggers for pricing flexibility correctly recognize that facilities- based

[6] USTA Comments, at 13.
[7] *See* BellSouth Comments, *passim*, SBC Communications Comments, *passim*, Verizon Comments, *passim*, and the attachments to all of those comments.
[8] AT&T Comments, at 2.

competitors serving customers (as shown by collocation or other facility deployment) in an area can serve a great many other customers in the same area once presented with requests for service. Therefore, the relevant area in which competitors discipline market prices is far greater than the individual routes on which they have won customers and installed circuits. Just because competitors have yet to put in particular circuits, or reach into particular buildings (particularly locations where there is only one potential customer), this does not negate the basic fact that these competitors can offer competing services to those buildings and build out to meet demand for their services.

A. Complaining Parties Fail To Support Their Claims with Evidence.

1. *Alleged Evidence of a Lack of Competition Is Entirely Consistent with Competition*

The fact that any given customer-specific route is not yet served by multiple facilities only shows that the customer has yet to switch providers, and not that the customer doesn't have a choice of providers. Often, a telecommunications provider will defer actual construction of facilities on any given route until after it has received a reasonable indication of interest in services. The fact that customer-specific DS-1 circuits must be installed before service can be initiated, therefore, does not prove that there are substantial barriers to entry permitting incumbents to realize monopoly profits. To the contrary, the sum of current and future demand is predictable and can be internalized by an alternative provider. Therefore, as Nobel Prize-winning economist George Stigler explained, the investment is not a barrier to entry and the service is contestable, preventing super-competitive prices.[9] In this regard, it is important to note that competitive markets price to *entrants'* incremental costs, so the many comparisons in the comments of prices with (flawed) estimates of USTelecom members' incremental costs of

[9] George Stigler, *The Organization of Industry* (1968).

providing services[10] are not particularly relevant to an analysis of competition in special access markets, unless there is some reason to believe that entrants necessarily are as efficient as, or more efficient than, USTelecom members. The record does not provide any foundation for such a conclusion.

2. No Reasonable Rebuttal Is Given Regarding the Unreliability of ARMIS Data

As explained in the USTA Comments, whether or not ARMIS data is useful for some purposes, it simply is not reliable for measuring service-specific profits.[11] Instead, one must look to the profits of the firm as a whole. By this measure, USTelecom members can hardly be said to be reaping monopoly profits and, indeed, rates of return are declining consistent with increased competition.[12]

ARMIS data is even less useful for setting just and reasonable rates. For example, it would have been completely inappropriate to use ARMIS for rate setting in Missouri in 2001. Looking at SBC's ARMIS data shows an entry of *negative* $1,724,000 for general and administrative expense on special access services in Missouri that year.[13] This was undoubtedly a proper entry under ARMIS rules, and it is not intrinsically wrong in an accounting sense to have a contra-cost category be larger than a cost category, which would produce such a result. It is economically impossible, however, for costs to be *negative*. The real-world implication of such a result would be that the firm would make money simply by engaging in the activity—for every unit of General and Administrative activity the firm produced, the company would have

[10] *See* note 2, *supra*.
[11] USTA Comments, at 11-12.
[12] Indeed, the Bell Operating Companies as a group, have seen their overall rates of return drop significantly, as shown by comparing their average rates of return for 1999-2001 (approx. 15.78%) with their average rates of return for 2002-04 (approx. 12.25%). *E.g.*, SBC Comments, Appendix C (Toti Declaration), Attachment 7.
[13] SBC Communications, *FCC Form 43-01*, SBC Missouri, Line 1160 (2001).

more money irrespective of whether that activity produced any revenue, directly or indirectly. To state it another way, if ARMIS were a reliable tool for estimating profits (and setting rates), SBC would have found the proverbial "money tree" in General Administrative activity within the state of Missouri.

Some parties allege that the Commission should not consider these basic and irrefutable arguments against using ARMIS data for rate making because, as these parties allege, USTelecom and its members somehow "waived" objections to this use of ARMIS data.[14] Even if there were any truth to these purported waivers of objections to misusing ARMIS, such a waiver would not apply to the Commission in this rulemaking, which is governed by the principles of administrative law. Instead, the Commission must make its own affirmative determination that rates are just and reasonable, so the Commission cannot simply find that objections to unreliable evidence have been waived and then use that evidence to reduce rates. To do so would be flagrantly arbitrary and capricious.

3. Allegations Regarding High Costs Actually Support the Reasonableness of Current Price Levels

As explained above, there are many competitors in special access markets, with many different assets and capabilities. Therefore, the costs of entry are not a barrier to entry. Special access, simply put, is *not* a natural monopoly. Nonetheless, those who seek re-regulation argue that entry is somehow too difficult for the Commission to rely on competitive markets to serve the public interest. These parties' arguments largely explain that special access circuits are costly to build, and that they are risky investments due to customer defections (both of which are factors that apply equally to USTelecom members as well).[15] While this evidence does not

[14] *E.g.*, ATX/Bridgecom/Broadview/Pac-West/US LEC/U.S. Telepacific Comments, at 8.
[15] *See* note 6, *supra*. In particular, NEXTEL describes how difficult, costly, and risky it is to

demonstrate inefficient market results, it does clearly show that special access services are neither cheap nor easy to provide. In effect, those seeking re-regulation are arguing that they find it too costly to build their own special access circuits or order them from competitors (who will have to install new circuits in many cases) at current rates. Rather than supporting the calls for greater price regulation, this evidence simply proves that current rates are just and reasonable, and that competition is working just fine.

II. RENEWED PRICE REGULATION WILL DETER COMPETITION, THEREBY HARMING THE PUBLIC INTEREST

The calls for regulatory-mandated price reductions, if heeded, will only slow the development of competition and will promote conditions that prevailed during the days of regulated monopoly. If as proponents of re-regulation allege, it is difficult and costly to build special access circuits at current price levels, then lowering prices further as they request will only make entry more difficult. Therefore, there is an inherent disconnect between the calls for re-regulation and the clear intent of Congress to promote competition and deregulation. Congress expressed its intent clearly in the Telecommunications Act of 1996, and this Congressional mandate was consistent with the Commission's own decades-old and successful policy of promoting competition in telecommunications markets, particularly special access markets. This history was described in detail in USTelecom's initial comments,[16] and the Commission must not turn back now on this successful history, which has produced innovation, lower prices, and improved service in all telecommunications markets.

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deploy channel terminations to cell cites and, in the process, notes factors that apply equally to incumbent LECs because they also must construct new facilities to reach remote cell towers. NEXTEL Comments, at 10.

[16] USTA Comments, at 6-8.

Moreover, as USTelecom explained in its initial comments in this proceeding, special access infrastructure requires substantial capital investment, which means that companies investing in special access facilities must be reasonably confident that they will realize lifetime returns commensurate with the risk of the investment.[17] If, instead, potential investors see current special access providers' returns drastically curtailed to comport with regulators' ideas about the returns they should have received, they will not take the risk of making these critical investments.

Because of the magnitude of the investment risk at stake, the Commission's decisions in this proceeding will affect more than just those companies that have made substantial investments in the past. These decisions also will have a powerful impact on future investment as the outcome will affect investor expectations for the foreseeable future. In brief, the Commission must recognize the value of companies' networks and allow markets rather than regulatory accounting to determine the appropriate return on investments.

Given the emphasis in the NPRM and parties' comments on alleged profit margins, it is worth reminding ourselves in this proceeding that the goal is a competitive market, and not a highly-regulated monopoly, even if the monopoly might produce modestly lower rates in the short run. Congress mandated competition and deregulation;[18] not the lowest prices, or the most modest profits. In fact, it should be expected that some rates will increase in competitive markets, and that margins on some services will be higher than in regulated markets, neither of which will make those rates unjust or unreasonable.

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[17] USTA Comments, at 3-4.

[18] Preamble to the 1996 Act, which can be found at Committee on Energy and Commerce, United States House of Representatives, *Compilation of Selected Acts within the Jurisdiction of the Committee on Energy and Commerce*, Communications Law at 413 (April 2003).

Even if some prices do not decline in the short run, the benefits of competition over the long run far outweigh any drawbacks and the Commission should stay the course it has been following for more than three decades, and not heed calls for a return to regulated monopoly. In particular, competition produces: (a) more efficient prices; (b) more innovation as competitors find ways to win customers; (c) lower firm-incurred and governmental administrative costs; (d) a reduced likelihood of errors in price setting; (e) greater adaptability to technological and market changes; and (f) more efficient preparation for technological and business risks.

Competitive markets do not operate efficiently if important market participants are precluded from responding to market price signals, particularly those putting downward pressure on prices. Some commenting parties oppose such pricing flexibility, arguing in particular, that USTelecom members are engaged in allegedly offering exclusionary terms and conditions for price discounts.[19] Rather than being anticompetitive, however, the tactics about which these parties complain generally are normal ways of addressing the inherent risks in high-capacity service markets. In fact, competitors are also using many of the same tactics in their effort to win customers away from USTelecom members and prevent its members from responding competitively in an effort to retain/regain special access business.

III. CONCLUSION

Special access markets are increasingly competitive, as shown by the evidence submitted in the comments filed in this docket on June 13, 2005. Rather than recognize these developments and embrace market prices, some special access customers are asking the Commission to re-regulate special access to produce lower prices in response to alleged evidence

[19] *E.g.*, American Petroleum Institute Comments, at 10-12; AT&T Comments, at 6-8; ATX/BridgeCom/Broadview/Pac-West/ US LEC/U.S. Telepacific Comments, at 35-39; CompTel/ALTS/Global Crossing/NuVox Comments, at 32-34;Time Warner Telecom Comments, at 21-25; WilTel Communications, at 19-20.

of above competitive profits realized by special access providers. This alleged evidence is based on ARMIS reports designed for other uses and it is inappropriate for ratemaking. Moreover, it is an utterly inadequate basis for rejecting the clear and substantial evidence of competition submitted by special access providers.

Even if special access markets were not competitive, price reductions would only make the situation *worse* as they would deter entry, particularly by firms using new technologies such as cable modems, Wi-Max/fixed wireless, and powerline broadband to provide true facilities-based competition for DS-1 circuits. Accordingly, the Commission should continue promoting competition and rewarding investment and efficiency. This can best be achieved by: (1) preserving current price cap levels; (2) allowing commercially-negotiated contracts everywhere; (3) declining to impose a productivity factor; and (4) declining to adopt interim rules.

Respectfully submitted,

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